

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

SPECIAL CIVIL APPLICATION No 2692 & 2694 of 1996

For Approval and Signature:

Hon'ble MR.JUSTICE R.BALIA.

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1. Whether Reporters of Local Papers may be allowed to see the judgements?
2. To be referred to the Reporter or not?
3. Whether Their Lordships wish to see the fair copy of the judgement?
4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder?
5. Whether it is to be circulated to the Civil Judge?

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(1) SPL. CIVIL APPLICATION NO. 2692 OF 1996

KARNAVATI FINCAP LTD

Versus

SECURITIES & EXCHANGE BOARD OF INDIA

(2) SPL. CIVIL APPLICATION NO. 2694 OF 1996

M/s. ALKA SPINNERS LTD.

VERSUS

SECURITIES & EXCHANGE BOARD OF INDIA

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Appearance:

MR SN Soparkar with MR BN KAKADIYA for Petitioners  
MR KN Raval & MR BH CHHATRAPATI for Respondent

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CORAM : MR.JUSTICE R.BALIA.

Date of decision: 06/05/96

COMMON ORAL JUDGEMENT

These two petitions raise identical issues and

are therefore, decided by this common order.

Petitioners have challenged issuance of summons to them by the Security & Exchange Board of India (For short SEBI )-respondent to appear before the Investigating Authority u/s. 11(3) of the SEBI Act. The contention of the petitioners is that under the provisions of the CEBI Act and under the provisions that have been referred to in the summons, petitioners can called upon to furnish information nor an enquiry can be made against them. Their case is that the petitioners in both the cases are purchasers of securities namely shares of Mr. Madanlal B Purohit listed at Stock Exchange, Bombay. Merely because as investors they have dealt with those shares through Stock Brokers at Stock Exchange, Bombay, they do not fall in category of person against whom inquiry can be instituted or from whom information can be called or discovery of documents can be made. Learned counsel for the petitioners in support of his arguments relies on the statutory provisions contained in section-11, sub-section 2 clause -(i) read with sections 11B and 12 of the SEBI Act. He contends that the combined reading of these provision leads to only one conclusion that only person who are covered by these provisions are stock exchanges, mutual funds, other persons associated with the securities market and intermediaries and self-regulatory organisations in the securities market. The persons referred to as "associated with the securities market", according to the learned counsel, refers only to persons enumerated in clause(ba) of sub-section 2 which has been inserted by the Securities Laws (Amendment) Act, 1995 with effect from 25.1.1995. His further contention is that section 11B confers on the SEBI power to issue directions in purusance of any inquiry. For the present purpose, his argument is that such directions can be issued to any person or class of persons referred to in section 12 and persons referred to in section 12 does not include the investors like the petitioners. To buttress this argument, a reference was also made to object of the bill for amending the Securities Laws in India.

Learned counsel for the respondent urged that reading of the provisions of section 11 without reading sub-section(1) and without referring to the provisions of (Prohibition of Fraudulent and Unfair Trade Practices releting to Securities Markets) Regulations, 1995 which have been framed under the powers conferred u/s.30 of the SEBI Act which has come into force after the same were placed before the Parliament for its approval, have a statutory force. It was also urged that object of SEBI

Act is to secure a check on the mal-practice prevalent in dealing of the securities to protect the interest of investors. The provisions which have been made to achieve this object should not be read in a narrow and pedantic manner but full effect should be given to the provision to make it effective to fulfil the object. It was also urged that if language of the statute is clear, reference to the object clause of the bill is not permissible. It was further urged that the power has been conferred in widest possible aptitude in the matter of calling of information in the form of statement or documents by extending provisions of Civil Procedure Code while trying a suit regarding discovery and production of the books of account and other documents and summoning and enforcing the attendance of persons and examining them on oath, apart from inspection of any books, registers and other documents of any person referred to in section 12 of the Act.

For examining the rival contentions, it would be appropriate to refer to the relevant provisions of sections 11, 11B and Section 12. Section 11 (1) imposes paramount duty on the Board to protect the interests of investors in securities and to promote the development of, and to regulate the securities market, and for achieving this object, it gives out plenary powers to have resort to such measures as it thinks fit. Section 11(1) not only prescribes duties but confers powers as well, to effectively discharge those duties. Viewed in this way, sub section (2) which commences with words "without prejudice to the generality of the foregoing provisions," proceed to enumerate matters for which the Board may provides such provision is to be read as illustrative and not exhaustive of the matters of the measures which can be provided for by the Board in furtherance of discharge of its duties referred to in sub section (1).

The words 'other persons associated with the securities market' have not been defined in the Act. The question then arises whether the persons associated with the securities market takes its colour from persons enumerated in clause (ba)? If one has to go by the literal meaning, the interpretation which restricts the meaning of "persons associated with the securities market" with the persons enumerated in clause (ba) is not acceptable. In ordinary meaning, the persons associated with the securities market would include all and sundry who have something to do with the securities market. It is to be noted that the securities market in the sense is not confined to stock exchanges only. The words 'persons

associated with the securities market' are of much wider import than intermediaries. 'Persons associated with' denotes a person having connection or having intercourse with the other; in the present case that 'other' with whom a person is to have connection or intercourse is the securities market. Term 'securities market' has not been defined under the statute. But taking the meaning of security as defined in Securities (Contract) Regulation Act, 1956 because that is the definition of the Securities adopted under the SEBI Act, and ordinary meaning of word 'market', it will mean a place or institution where business of selling or buying of securities is carried on. Selling, buying or dealing with securities is the essential ingredient of a market. Though securities market has not been defined, definition of 'Stock Exchange' under section 2(i) of the Securities Contract (Regulation) Act means any body of individuals whether incorporated or not, constituted for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities. Security has been defined under section 2(h) to include shares, scripts, stocks, debentures, debentures stock or other marketable securities of like nature in or of any incorporated company or other body corporate etc. etc. What is noticable in it refers to 'marketability' of it. Stock Exchange is more than a mere selling, buying or dealing place for securities, but adorns the role of an assisting agency in smooth conduct of securities business by suitable regulating or controlling authority. None the less a market cannot be conceived without a seller or buyer who are the primary persons for whose purpose the market exists. All activities of business of selling and buying are related to seller or buyer. It is inconceivable to think that a buyer or seller of a script is not a person associated with securities market, where or through which he transacts his business, whether as trader or as investor, of selling or buying the required script.

Even taking narrower view as suggested by the learned counsel for the petitioners, by restricting the meaning of persons 'associated with the securities market' only to that class of persons referred to in clause (ba) does not keep out the primary persons in the dealing of the securities out of inquiries as contemplated in clause (i) of section 11(2). What is contemplated is calling for information from the persons enumerated in clause (i) and, also conducting inquiries in the affairs of stock exchanges, mutual funds and other persons associated with the securities market and intermediaries and self-regulatory organisations in the

securities market. The provision is two fold. Firstly, calling for information primarily before holding any inquiry , and, secondly holding of an inquiry into the affairs of the persons named therein and transactions in securities which takes place under its precincts or through its agencies. While calling for information, a power may be restricted to the persons enumerated therein. But where calling for the information is incidental to the conducting of the inquiries into the affairs of stock exchange or persons associated with stock exchange than persons to whom such an inquiry would reach cannot be restricted. It would be self defeating to hold that the investigation into any mal-practice attached with any transaction or practice carried in stock exchange can be made only up to intermediary but cannot reach the primary source of transaction. It will be like searching for light in a tunnel without reaching its mouth. All the persons connected with the subject of enquiry are amenable to its reach.

Therefore, once an inquiry is to be conducted with respect to any securities dealt with at the stock exchanges or of any persons connected with such securities, whether the primary dealers or intermediary dealers and whether there was broker or the share transfer agent or in any capacity associated with the conduct of such transactions fall within the scope and ambit of inquiry under sec. 11(2)(i) and, if anybody is found involved in any mal-practice, it would be within the reach of Board to issue directions under section 11A.

Section 11B also enumerates the persons 'associated with the securities market' to whom directions can be issued. What is stated in respect of interperitting of meaning of 'persons associated with the securities markets' under section 11(2)(i) equally applies to it.

Regulations of 1995 sheds doubts, if any, about ambit of authority of SEBI regarding calling of information and holding of inquiry. The framing of regulations is empowered by section 30 which reads as under:

Section:30 : Power to make regulations:

- (1) The Board may, with the previous approval of the Central Government, by notification, make regulations consistent with this Act and the rules made thereunder to carry out the purposes

of this Act.

(2) In particular, and without prejudice to the generality of the foregoing power, such regulations may provide for all or any of the following matters, namely:-

(a) xxx xxx xxx

(b) xxx xxx xxx

(c) the matters relating to issue of capital,  
transfer of securities and other matters  
incidental thereto and the manner in  
which such matters shall be disclosed by  
the companies under section 11A.

(d) xxx xxx xxx

Section 31 provides that every rule or regulations made under the Act shall be laid before each House of Parliament while in session, as soon as for a period of 30 days after such rule or regulation is made. If both the houses agree for any modification, then such rule or regulation will operate only in its modified form. If both the Houses agree that such rule or regulation is not to be made, it ceases to be in operation. These provisions clearly show that regulations are of legislative in nature and statutory in character, and bears the seal of approval by the Parliament, after they are made for their continued existence.

The purpose of act as indicated in the preamble is to provide for the establishment of the Board to protect the interest of investors in securities and to promote the development of and to regulate the securities market and for matters connected therewith or incidental thereto. Section 11 casts a duty on the Board to protect the interests of investors in securities and to promote the development of and to regulate the securities market. For achieving such object, it has been authorised to take such measures as it thinks fit. Thus power to take all measures necessary to discharge its duty under Statute which is reflection of objective disclosed in the preamble has been conferred in widest amplitude. Protecting interests of investors in securities and healthy development of securities market takes within its sweep all measures to effectively tackle the mal-practices connected with security trading meant for manipulating market prices for ulterior motives of inducing the investors in selling or purchasing

securities at such manipulated and artificial market conditions. In furtherance of this object to keep check on such manipulative or fraudulent transactions which are not bonafide and genuine transactions of sell and purchase but a part of manipulative mechanism the Board had framed ( Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995 by publishing the same in Gazette of India, Extra ordinary dated 25.10.1995 which were laid before Parliament and are in existence in the present form.

Regulation-3 prohibits buying or selling of or dealing with securities in a fraudulent manner. Regulation-4 prohibits manipulative trade practices which includes entering in any transactions with intention of artificially raising or depressing the prices of securities thereby inducing other persons to sell or buy securities; which is calculated to create a false or misleading appearance of trading in securities market; which results in reflection of prices of securities based on transaction that are not genuine trade transactions; which are not intended to effect transfer of beneficial interest of ownership but intended to operate only as a device to inflate, depress or cause fluctuation in market price of securities; pay off for inducing another person to purchase or sell the security with the sole object of inflating, depressing or causing fluctuations in market price of securities.

Regulation 5 prohibits making of misleading statements in material particulars whether deliberately or without due care and caution, which is likely to induce other persons to purchase or sell their securities or affect market prices of securities. Regulation 6 prohibits fraudulent and Unfair Trade Practices.

Laying down these norms to achieve their compliance and to achieve its paramount object, Regulation-7 empowered the Board to investigate in buying and selling of securities, and Regulation- 8 provided procedure for such investigation. Regulations 7 & 8 read as under:

Regulation : 7(1)The Board may, suo-motu or upon information received by it, cause an investigation to be made in respect of the conduct and affairs of any person buying, selling or otherwise dealing in securities, by an investigating officer whom the Board considers fit.

Provided that no such investigation shall be made

except for the purposes specified in sub-regulation (2).

(2) The purposes referred to in sub-section (1) are the following, namely:-

- (a) to ascertain whether there are any circumstances which would render any person guilty of having contravened any of these regulations or any directions issued thereunder;
- (b) to investigate into any complaint of any contravention of the regulation, received from any investor, intermediary or any other person;

Regulation : 8(1) Before causing an investigation to be made under regulation 7, the Board shall give notice.

(2) Notwithstanding anything contained in sub-regulation (1), where the Board is satisfied that in the interest of the investors or in the public interest, no such notice should be given, it may, by an order in writing and recording the reasons as far as practicable, direct that the investigation be undertaken without such notice.

(3) Subject to the provisions of this regulation, an order passed under regulation 7 shall be a sufficient authority for the Investigating Officer to undertake the investigation and, on production of an authenticated copy of the order, the person concerned shall be bound to carry out the duty imposed in regulation 9.

Regulation-9 casts a duty on the person concerned to co-operate and furnish requisite information and documents. Regulations -11 and 12 provide for issuing directions to buyers and sellers in respect of any transaction which has taken place in contravention of the Regulations after report of enquiry has been submitted to the Board.

These provisions cannot be said to be inconsistent with any provision of the Act or Rules framed thereunder. In fact, no such contention was raised, except that summons under section 11(3) could not have been issued to buyer while holding inquiry under



section 11(2)(i).

Firstly, as I have discussed hereinbefore, the enquiry cannot be said to be beyond the scope of section 11(2)(i). Even assuming for the present purpose, that section 11(2)(i) does not contemplate any enquiry against a buyer or purchaser, the list of measures enumerated in sub section (2) of section 11 is merely of illustrative nature of measures that may be taken by the Board in furtherance of its duties and attain the object of the statute, without affecting the generality of provisions of sub section (1). It cannot be said that sub section (2) provides an exhaustive list of measures which the Board can take and it cannot take other measures which are in consonance with the main purpose of the statute and consistent with the duty cast on it. It cannot be said that for protecting the interests of investors, the Board has no power to take appropriate measures to prevent and deal with fraudulent and manipulative transactions. The Board has such powers, nay duty, to take measures to prohibit unearthen and deal with fraudulent and manipulative transactions to effectively protect the interests of investors. This is also necessary in order to promote healthy, fraud free and manipulative free development of securities market in the Country that effective measures are taken to check and prevent transactions which tend to artificially affect and manipulate market conditions to the advantage of a few and to the detriment of general genuine investors. Therefore, no prohibition can be read in the provisions of section 11(2) for not giving effect to Regulations of 1995.

Regulations of 1995 in no uncertain terms provide for an investigation in respect of the conduct and affairs of any person buying, selling or otherwise dealing in securities.

Thus, necessary power to hold enquiry against buyer or seller and power to call for information from him exists. The fact that in summons reference has not been made to these Regulations is immaterial. Such omission by itself does not invalidate the exercise of authority. Law in this regards is well settled that if source of power exist, non mentioning of it or wrong labelling of it would not invalidate exercise of such powers.

I am unable to sustain the contention of the petitioners that the Board has no power to conduct an

inquiry in the transaction of transfer of shares by the petitioners and inquiry of the Board must stop at the stock brokers or intermediaries who have been instructed to carry out the transactions of petitioners.

Contention that the information cannot be called from the petitioners because clause 11(2) restricts calling for information from undertaking inspection, conducting inquiries and audits of the stock exchanges, mutual funds, other persons associated with the securities market and self-regulatory organisations in the securities market only and the petitioners does not fall in any of them must also fail.

The contention that no enquiry can be held against petitioner buyer has been rejected on two grounds namely; (I) the buyer does fall within the purview of class enumerated in clause (i) as person associated with securities market and (II) that Regulations of 1995 specifically provides for holding investigation in conduct and affairs of any buyer or seller in respect of transaction referred to in Regulations 3 to 6, even if it is assumed that he does fall outside the purview of persons associated in transaction which have been the subject matter of inquiry. In either case, once an inquiry is to be conducted as to who are the persons responsible for the mal-practice falling within the purview of inquiry and if they otherwise fall within the subject matter of inquiry then in that event, they are subject to the powers as are conferred on a civil court in the matter of discovery and production of documents and summoning and enforcing the attendance of persons and examining them on oath. In this connection, section 30 of the Code of Civil Procedure reads as under:

Section : 30:C.P.C. Power to order discovery and the like:

Subject to such conditions and limitations as may be prescribed, the Court may, at any time, either of its own motion or on the application of any party,-

(a) make such orders as may be necessary or reasonable in all matters relating to the delivery and answering of interrogatories, the admission of documents and facts, and the discovery, inspection, production, impounding and return of documents or other material objects producible as evidence;

(b) issue summons to persons whose attendance

is required either to give evidence or to produce documents or such other objects as aforesaid;

(c) order any fact to be proved by affidavit.

Section 30 empowers the court on its own motion to issue summonses to person whose attendance is required either to give evidence or to produce documents or such other objects as aforesaid, that is to say, that persons whose attendance is necessary and relevant for the purposes of inquiry at any time, or in whose possession the relevant documents are there, the civil court has necessary jurisdiction and power to summon such a persons and enforce his statement as well as production of documents relevant for the inquiry. Such person may or may not be a person against whom suit has been filed or relief has been claimed or is otherwise party to the suit. Therefore, power to call for information and documents relevant for the inquiry even from the persons against whom inquiry has not been instituted and/or cannot be instituted vests in the SEBI or in the person authorised to hold enquiry in terms of section 11(3). Exercise of such powers cannot be confined to the persons enumerated in clause(i) of section 11(2). To hold otherwise will be to infructuate the purpose of holding the inquiry by keeping out of reach of the inquiry authority, relevant documents and evidence which can be said to be of primary importance for the enquiry and required by the authoity for the purpose of such enquiry.

For the reasons as aforesaid, both these petitions fail and are hereby dismissed. Notice discharged in each case. No costs.

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